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No. 92-1621

In the Supreme Court of the United States

OCTOBER TERM, 1992

A. JOYCE PAYNE, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether wages paid to United States citizens by the Panama Canal Commission are exempt from federal income taxation under Section 911 of the Internal Revenue Code.

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OPINIONS BELOW

The opinion of the district court (Pet. App. 1a-36a) is reported at 778 F. Supp. 804. The opinion of the court of appeals (Pet. App. 1b-26b) is reported at 980 F.2d 148.

JURISDICTION

The judgment of the court of appeals was entered on November 25, 1992. On February 22, 1993, Justice Thomas extended the time for filing a petition for a writ of certiorari to and including March 25, 1993. The petition for a writ of certiorari was filed on March 25, 1993. The jurisdiction of this court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. During 1982, Arthur C. Payne was an employee of the Panama Canal Commission ("PCC") and resided in the Republic of Panama. He received wages of $75,780 from the PCC in that year. Mr. Payne and his wife (the petitioner in this case)[1] were United States citizens and were therefore required to file a United States income tax return. In submitting their joint return for 1982, however, they excluded the PCC wages from taxable income on the ground that the Panama Canal Treaty exempted PCC wages from federal taxation (Pet. App. 2a, 5b).

The Internal Revenue Service determined that Mr. Payne's PCC wages were not excludable from taxable income and, on March 10, 1986, made an assessment of $24,457 in tax and $9,477.90 in interest with regard to the Paynes' 1982 tax year (Pet. App. 2a-3a).[2] Petitioner did not pay the assessment. The Service therefore levied upon funds in her bank account and applied those funds to her tax liability (Pet. App. 3a, 6b-7b). Petitioner filed a claim for refund and then commenced this refund action in federal district court (Pet. App. 4a, 7b).[3]

Petitioner contended that PCC wages were exempt from United States taxation under Section 911 of the Internal Revenue Code (as "foreign earned income") and

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[1] Mr. Payne died in 1985 (Pet. App. 6b).

[2] An assessment was also made with regard to the Paynes' 1981 tax year (Pet. App. 2a-3a, 6b), but that year is not at issue here.

[3] The amount seized by the government's levy satisfied in full petitioner's unpaid tax liability but not the assessed interest. Because the tax obligation was fully paid, the district court had jurisdiction over petitioner's suit even though some of the interest remained unpaid. See *Flora* v. *United States*, 362 U.S. 145, 171 n.37 (1960). The United States filed a counterclaim for the balance of the interest (Pet. App. 4a-5a, 7b-8b).

that the exception to that statute for wages paid by a United States agency (26 U.S.C. 911(b)(1)(B)(ii)) did not apply to PCC employees because the PCC was not an agency of the United States (Pet. App. 6a, 8b).

2. The district court granted summary judgment to the United States. The court held that "there is little question the PCC is an agency of the United States" (Pet. App. 13a). In reaching this conclusion, the court looked to the legislation establishing the PCC and to the degree of control that the United States maintains over the PCC (Pet. App. 13a-26a). The court stated that the factors emphasized in *Kalinski* v. *Commissioner*, 528 F.2d 969 (1st Cir. 1976), and *Morse* v. *United States*, 433 F.2d 1185 (Ct. Cl. 1971), cert. denied, 405 U.S. 989 (1972), require the conclusion that the PCC is an agency of the United States and that the wages earned by petitioner's late husband from the PCC were therefore subject to federal income tax under 26 U.S.C. 911(b)(1)(B)(ii) (Pet. App. 25a-26a, 35a-36a).

The court of appeals affirmed (Pet. App. 1b-26b). Applying the factors set forth in *Kalinski* v. *Commissioner*, *supra*, the court held that the PCC was "under the control of the United States and must be considered an agency under § 911" (Pet. App. 21b). The court therefore concluded that the PCC wages received by petitioner's husband were subject to the federal income tax (*ibid.*).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or of any other court of appeals. Further review is therefore not warranted.

The world-wide income of United States citizens is subject to taxation by the United States regardless of the citizen's residence or the source of such income. 26

U.S.C. 1. See *Cook* v. *Tait*, 265 U.S. 47, 56 (1924). Section 911(a)(1) of the Internal Revenue Code provides, however, that, "[a]t the election of a qualified individual * * *, there shall be excluded from the gross income of such individual, and exempt from taxation * * *, the foreign earned income of such individual." 26 U.S.C. 911(a)(1). Section 911(b)(1)(B) of the Code, however, excludes from the definition of "foreign earned income" all amounts "paid by the United States or any agency thereof to an employee of the United States or an agency thereof" (26 U.S.C. 911(b)(1)(B)(ii)).

The courts below correctly rejected (Pet. App. 12a-28a, 35a-36a, 10b-26b) petitioner's contention that the Panama Canal Commission is not a United States agency and that wages paid by the PCC to United States citizens are exempt from federal income taxation as foreign earned income under Section 911. The 1977 Panama Canal Treaty (Treaty) states that "the United States of America shall * * * carry out its responsibilities [under this treaty] by means of a United States Government agency called the Panama Canal Commission, which shall be constituted by and in conformity with the laws of the United States of America" (Pet. App. 24c; Treaty Art. III, ¶ 3). The statute enacted to establish the PCC further emphasizes that the PCC is a United States agency: "There is established in the executive branch of the United States Government an agency to be known as the Panama Canal Commission" (22 U.S.C. 3611).

Courts have consistently recognized that the PCC is a United States agency. For example, this Court stated that the PCC is a "United States Government agency" in *O'Connor* v. *United States*, 479 U.S. 27, 28 (1986), as did the Fifth Circuit in *McGehee* v. *Panama Canal Comm'n*, 872 F.2d 1213, 1215 (1989). The Tax Court, addressing the specific issue involved in this case, held

that the PCC is an agency of the United States for the purposes of Section 911 in *McCain* v. *Commissioner*, 81 T.C. 918, 924 (1983).

Even setting aside the plain language of the Treaty and the legislation establishing the PCC, the PCC would qualify as an agency of the United States under the general test adopted by the courts, which looks "to the degree of control the government exercises over the entity" (Pet. App. 16a, 10b-11b). Courts have looked to the four factors specified and evaluated in *Kalinski* v. *Commissioner*, 528 F.2d at 973, and *Morse* v. *United States*, 443 F.2d at 1188, for this purpose: (i) the power of the United States to initiate and terminate the entity, (ii) whether the entity effectuates governmental purposes, (iii) whether the entity generates private profits, and (iv) whether employment at the entity is limited to persons connected with the government. Petitioner agrees that these are proper factors to consider (Pet. 9-10), but differs with the lower courts in their application.

The courts below correctly applied these factors to conclude that the PCC is an agency of the United States. The PCC was created by legislation enacted by the United States Congress (22 U.S.C. 3601-3871) and will cease its operations under the terms of the Treaty to which the United States is a party (Pet. App. 20a; Treaty Art. II, ¶ 2). The United States has primary authority over the hiring and firing of employees of the PCC (Pet. App. 52c-63c; Treaty Art. X), as well as over the appointment and removal of the Administrator and Deputy Administrator and of the members of the Supervisory Board (Pet. App. 25c-27c; Treaty Art. III, ¶ 3(a)-(d)). A majority of the members of the Supervisory Board must be United States nationals (Pet. App. 25c; Treaty Art. III, ¶ 3(a)), and those members are required to vote as directed by the United States Secretary of Defense (22

and the fact that a high percentage of governmental funds came for the United States were sufficient indicia of United States control to find the Trust Territory was an agency of the United States for purposes of Section 911.

Although we believe there are sufficient indicia of control to find the Trust Territory was a United States agency for purposes of Section 911 we see no need to confirm our suspicion by conducting such an analysis here. Rather, we note each court's

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agreement. The Trust Territory's status as a strategic area places related matters before the Security Council. Since the United States has the power to veto affirmative acts of the Security Council it can insulate itself from affirmative acts of the United Nations with respect to its administration of the Trust Territory. See Groves 533 F.2d at 1384 n. 13.

methodology was consistent with the other's and our own. There was merely a disagreement over how to analyze the relevant facts. We see little similarity between the PCC, which is directly controlled by the Secretary of Defense, and the Trust Territory of the Pacific Islands, which is arguably a foreign sovereign operating under the wing of the United States, and therefore find McComish unpersuasive on the issue of whether the PCC is an agency of the United States.[14]

CONCLUSION

We find the Panama Canal

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[14]Nor does the apparent conflict between Groves and McComish alter our belief we have sufficient information regarding the operation of the PCC to make the determination it is an agency of the United States.

Commission is an agency of the United States and therefore, 26 U.S.C. Section 911 does not exempt from federal income taxation wages the PCC pays its employees who are United States citizens. Payne's 1982 income is subject to federal income taxation and she is liable for any amount due. For the foregoing reasons, the motion of the United States for summary judgment is granted.

The Clerk of Court shall enter judgment for the United States. No costs.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 235 August Term 1992
(Argued Nov 5, 1992
Decided Nov. 25, 1992)

Docket No. 92-6017

A. JOYCE PAYNE,

Appellant,

v.

UNITED STATES,

Appellee.

Before:

TIMBERS, VAN GRAAFEILAND, and McLAUGHLIN, Circuit Judges.

Appeal from a summary judgment entered in the District of Vermont, Albert W. Coffrin, Senior District Judge, 778 F. Supp. 804 (D. Vt. 1991), holding that the Panama Canal

Commission qualifies as an agency of the United States for purposes of 26 U.S. C. §911 (1988), and that wages paid to its employees, including appellant's husband, were not excludable from taxable income as foreign earned income.

Affirmed.

Rober A. Gensburg, St. Johnsbury, VT, for appellant.

David E. Carmack, Atty., Tax Division, Dept. of Justice, Washington, D.C. (James A. Bruton, Acting Asst. Atty. Gen., Gary R. Allen and Randolph L. Hutter, Attys., Tax Division, Dept. of Justice, Washington, D.C.; and Charles A. Caruso, U.S. Atty., Rutland, VT, on the brief), for appellee.

TIMBERS, Circuit Judge:

In this case of first impression at the appellate level, appellant A. Joyce Payne appeals from a summary

judgment in favor of the United States and against Payne, entered in the District of Vermont, Albert W. Coffrin, Senior District Judge, 778 F. Supp. 804 (D.Vt. 1991). The Court held, as a matter of law, that the Panama Canal Commission ("PCC" was an agency of the United States Government, and therefore, wages paid to employees of that agency, including appellant's husband, are not excludable from taxable income under 26 U.S.C. §911 (1988), which exempts from taxation foreign earned income of citizens living abroad, unless such income is received from the United States or an agency thereof.

On appeal, Payne challenges the summary judgment, claiming that the PCC

is not an agency of the United States Government, and thus any income earned by employees of the PCC is exempt from taxation under §911. She further claims that, even if the PCC does qualify as an agency of the United States, the income earned by its employees is not paid by the United States or an agency thereof, and therefore is exempt under §911. Finally, she claims that summary judgment was improperly granted.

We reject all of Payne's claims on appeal and affirm the summary judgment in favor of the United States.

I.

We summarize only those facts and prior proceedings believed necessary to an understanding of the issues raised

on appeal.

In 1981 and 1982, appellant's husband was a United States citizen employed by the PCC. Appellant and her husband resided in Panama. The couple filed a joint United States income tax return for those years, excluding from their taxable income the amount Mr. Payne earned from the PCC. They claimed that this income was exempt under the Panama Canal Treaty of 1977 ("Treaty").

The Paynes also believed that, aside from to the Treaty, the income also was exempt under §911 of the Internal Revenue Code. This provision exempts from taxation foreign earned income of citizens residing abroad, unless the income is paid by the United

States or an agency thereof. 26 U.S.C. §911(b)(1)(B)(ii) (1988).

Mr. Payne died in 1985. On March 10, 1986, the IRS assessed $106,672.88 against the Paynes, representing unpaid taxes for the tax years 1981 and 1982. Of this sum, $33,934.90 represented back taxes and interest for 1982. On November 4, 1986, the Supreme Court held that the Treaty did not bar the United States from taxing wages paid to employees of the PCC. O'Connor v. United States, 479 U.S. 27 (1986) (Treaty only exempts PCC employees from Panamanian taxes). Appellant, nevertheless, did not pay the assessment. In February 1987, the IRS levied on her bank account, obtaining $32,630.49 in partial satisfaction of

the assessment.

Appellant in April 1987 first commenced this action in the district court to recover the levied funds. The court granted summary judgment in appellant's favor as to the 1981 taxes, based on the IRS' failure to follow proper procedure in levying upon those funds. The court did not address the issue of whether the PCC wages were exempt from taxation under §911. It dismissed the claim involving the 1982 taxes because of appellant's failure to exhaust her administrative remedies.

In April 1989, appellant, having exhausted her administrative remedies, commenced this action, once again seeking a refund of the levied funds, plus interest, for the 1982 taxes. The

United States counterclaimed to reduce the assessment to a judgment. It moved for summary judgment because appellant admitted that she and her husband filed a joint tax return, making her personally liable for any deficiency on the return. Following O'Connor, the court held that the Treaty did not create a tax exemption. Appellant, however, claiming that O'Connor did not hold that the PCC was an "agency" under §911, asserted that she qualified for that exemption from taxation.

The district court, after a hearing on the motion for summary judgment, held that, although O'Connor was not controlling on the issue of the §911 exemption, the legislation which created the PCC and case law which

discusses what constitutes an agency of the United States show that the PCC is an agency, thus creating United States income tax liability for employees of the PCC.

On appeal, appellant contends that she never had an opportunity to develop a factual record to show why the PCC is not an agency within the meaning of §911, and that the order granting summary judgment was not appropriate.

II.

It is common ground that a court shall grant summary judgment if there is no genuine issue of material fact, and the moving party is entitled to judgment as a matter of law. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 247 (1986). Thus, if the PCC is an

agency, appellant is liable for her 1982 taxes as a matter of law, and summary judgment was appropriate.

(A) The PCC is an Agency of the United States

No other court at the appellate level has addressed the issue of whether the PCC is an agency. But see McCain v. Commissioner, 81 T.C. 918 (1983) (Tax Court held that the PCC is an agency for purposes of §911). Both parties here agree that the proper test for determining what constitutes an agency is one which measures the degree of control the government exercises over the entity involved. Factors to be examined include: (1) power of the United States to initiate and terminate; (2) effectuation of government purposes by the entity; (3)

exclusion of private profit; and (4) limitation of employment to government-connected persons. Kalinski v. Commissioner, 528 F.2d 969, 973 (1 Cir. 1976); Morse v. United States, 443 F.2d 1185, 1188 (Ct. Cl. 1971), cert. denied, 405 U.S. 989 (1972).

Appellant contends that the PCC fails the first part of the control test in that the United States neither created nor has the power to dissolve the PCC. Appellant claimed at oral argument before us that the district court ignored the Treaty. She asserted that it was the Treaty, a joint undertaking between the United States and Panama, which actually created the PCC and that the Treaty states that the PCC shall remain in existence through

1999. Panama Canal Treaty, art. III, §3(a). Thus, so her argument goes, the United States does not have the power to terminate the PCC.

This argument, however, requires a narrow reading of the terms "initiate" and "terminate." Although the Treaty required the United States to create the PCC, the plain language of the Treaty refers to it as "a United States Government agency...which shall be constituted by and in conformity with the laws of the United States of America." Treaty, art. III, §3. The PCC was created by legislation enacted by the United states Congress which established the laws and procedures under which the PCC operates. 22 U.S.C. §§3601-3872 (1988 & Supp. 1992).

The language of the legislation makes it clear that the PCC is an agency in the Executive Branch of the United States Government, operating under the authority of the President as exercised through the Secretary of Defense. 22 U.S.C. §3611 (1988). The Secretary of Defense can direct how United States nationals on the supervisory Board of the PCC shall vote. 22 U.S.C. §3612(a) (1988). The legislation further requires that at least five of the nine Board members be United States nationals, the Secretary of Defense effectively controls the outcome of any decision of the Board. Even though the United States cannot technically terminate the PCC, it can terminate any decision or action of the

PCC.

Further, it is the President who, with the advice and consent of the Senate, shall appoint the United States nationals who are members of the PCC supervisory Board. This gives the United States control over the appointment of the majority of the Board. And although Panamanians propose their nationals for the Board, the United States actually makes the appointments and controls which of the proposed members are selected. Finally, regardless of the nationality of a Board member, it is the President who appoints and can terminate the administrator and the deputy administrator. 22 U.S.C. §3613 (1988). Based on these factors, even if the

Treaty technically may have created the PCC, the Untied States has tremendous control over initiating and terminating the membership and policies of the PCC.

The next question for determining if the PCC is an agency is whether it was established to effectuate government purposes. The plain language of the Treaty is convincing. It states that "[T]he United States of America shall...carry out its responsibilities [under the Treaty] by means of a United States Government agency called the Panama Canal Commission...." Treaty, art. III, §3.

This language shows that the PCC was established to effectuate the government's responsibilities and duties under the Treaty, and not, as

appellant asserts, to act solely as a managing agent and trainer for Panamanians before the final transfer of the Panama Canal. The United States, in operating the Canal, is performing the governmental exercise of the power of Congress to regulate commerce; it is not performing a purely proprietary or business activity for the government. Rogers v. Graves, 299 U.S. 401, 406 (1937), overruled on other grounds by Graves v. New York, 306 U.S. 466 (1939); McGehee v. Panama Canal Comm'n, 872 F.2d 1213, 1218 (5 Cir. 1989).

The third element which establishes the United States' control over an agency is whether it generates government revenue as opposed to

private profits. The statute, 22 U.S.C. §3712(c)(1)(1988), requires the PCC to deposit all of its receipts in the Panama Canal Revolving Fund, a part of the United States Treasury. Such funds cannot be expended without authorization by law. Even if the PCC operates at a profit, the assets can be used only to carry out the purposes of the PCC and cannot be spent without specific authorization of law.

Appellant asserts that payments made by the PCC to the Republic of Panama, as agreed to under the Treaty for use of its natural resources, constitute a private profit. Appellant says that a private profit is earned unless all revenues are for the benefit of the United States. Aside from the

fact that the republic of Panama is not a private entity, we reject this assertion because the payments to Panama are for government services and there is no evidence of private profit being generated by the PCC.

The final factor in determining whether the PCC is an agency is whether its membership is limited to government-connected persons. There is no specific definition of who is "government-connected." Appellant asserts that, since there are Panamanians on the Board who are employed by the PCC (with their number to increase over the term of the PCC), such employees cannot be government-connected.

In making this assertion,

appellant ignores the fact that the PCC employees are subject to the same duties and responsibilities as federal employees, and that the PCC legislation creates a code of conduct which is substantially similar to the laws applicable to federal employees. In fact, the President established the Panama Canal Board of Appeals, which makes the "final and conclusive" determination for employee grievances about job classification and pay rates. 22 U.S.C. §§3660-3662 (1988). Further, it is the Federal Labor Relations Authority which handles disputes between the PCC and the employees' union. Panama Canal Comm'n v. Federal Labor Relations Auth., 867 F.2d 905 (5 Cir. 1989). Moreover,

United States citizen employees of the PCC, under certain conditions, are eligible for federal benefits such as civil service retirement, disability, and death benefits. 22 U.S.C.§3649 (1988). These factors provide sufficient evidence of a government connection to the employees of the PCC. The PCC thus complies with the final prong of the test for control

Appellant compares the PCC to the Trust Territory of the Pacific Islands ("TTPI"), which the Ninth Circuit held was not an agency. McComish v. Commissioner, 580 F.2d 1323 (9 Cir. 1978). But see Groves v. United States, 533 F.2d 1376 (5 Cir.), cert. denied, 429 U.S. 1000 91976) (holding that the TTPI is an agency) even if we

were to agree that the TTPI is not an agency, it is sufficiently different in character to distinguish it from the PCC. The TTPI is a quasi-sovereign territory with its own tripartite government. McComish, supra, 580 F.2d at 1329. Unlike the TTPI, the PCC is not a sovereign or even quasi-sovereign body; it is subject to the laws of the United States. This analogy therefore is not dispositive.

We hold that the PCC is under the control of the United States and must be considered an agency under §911. Employees of the PCC are not exempt from paying United States income taxes.

(B) Appellant's Income Was Paid by an Agency of the United States

Appellant also claims that, even if the PCC is an agency, her husband

was not paid by that agency. She bases this on the fact that the PCC funds, which paid the salary, came from revenues from the Canal's operation. Since the funds did not come directly from the United States government, she says that it was not the United States (or an agency thereof) that paid her husband.

We reject this claim based on legal precedent in this area. Whenever an employee of the United States or any agency thereof receives wages from such an employer, the source of the wages is irrelevant; the employee is not exempt from paying taxes under §911. C.I.R. v. Mooneyhan, 404 F.2d 522, 527 (6 Cir. 1968) (although a foreign country was the source of funds, as an employee of

the United States one is paid by an agency of the United States and cannot seek §911 exemption), cert. denied, 394 U.S. 1001 (1969). Here, it was the PCC, an agency of the United States, which paid Mr. Payne's wages. The Treaty itself refers to the United States as the employer of PCC personnel. Congress regulates the wages for PCC employees. 2 U.S.C. §§3655-57, 3665 (1988). It is irrelevant that the funds for these wages did not come directly out of United States taxpayers' pockets.

Appellant cites Krichbaum v. United States, 138 F. Supp. 515 (E.D. Tenn. 1956), for the proposition that the §911 exemption applies when a foreign government's funds pay a United

States agency employee's salary. The instant case is readily distinguishable from Krichbaum. In Krichbaum, the foreign country was responsible for providing the employee's salary. Here, it is the United States which ultimately is responsible for paying the employees of the PCC.

(C) Summary Judgment Was Properly Granted

Appellant also asserts that summary judgment was not appropriate here because the Government did not file an affidavit proving that the amount appellant owed in taxes was calculated correctly. Appellant cites Fed. R. Civ. P. 56(c) in support of her assertion that the Government should have filed an affidavit to show that there is no genuine issue of material

fact. Appellant neglects to mention Fed. R. Civ. P. 56(e) which provides:

> "When a motion for summary judgment is made and supported as provided in this rule, an adverse party may not rest upon the mere allegations or denials of the adverse party's pleading[s], but the adverse party's response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial."

It is the adverse party to a motion for summary judgment who bears the burden of providing affidavits which set forth specific facts showing that there is a genuine issue for trial. Here, appellant made only a blanket denial in response to the Government's claim for the amount of taxes owed. It was the appellant who did not meet her burden in proving there was a genuine issue of

material fact. Summary judgment accordingly was properly granted.

III.

To summarize:

We hold that the district court properly held that the PCC is an agency under the test of control, and that it is the PCC, acting in its role as an agency of the Government, which paid the salary of its employees. The income earned as an employee of the agency is not exempt under §911. There being no genuine issue of material fact, summary judgment was appropriate.

Affirmed.

BY THE PRESIDENT OF THE UNITED STATES
OF AMERICA
A PROCLAMATION

CONSIDERING THAT:

The Panama Canal Treaty was signed at Washington on September 7, 1977, the text of which is hereto annexed;

The Senate of the United States of America by its resolution of April 18, 1978, two-thirds of the Senators present concurring therein, gave its advice and consent to ratification of the Treaty, subject to the following:

(a) RESERVATIONS:

(1) Pursuant to its adherence to the principle of non-intervention, any action taken by the United States of America in the exercise of its rights to assure that the Panama Canal shall remain

open, neutral, secure, and accessible, pursuant to the provisions of the Panama Canal Treaty, the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal, and the resolutions of ratification thereto, shall be only for the purpose of assuring that the Canal shall remain open, neutral, secure, and accessible, and shall not have as its purpose or be interpreted as a right of intervention in the internal affairs of the Republic of Panama or interference with its political independence or sovereign integrity.

(2) The instruments of ratification of the Panama Canal

Treaty to be exchanged by the United States of America and the Republic of Panama shall each include provisions whereby each Party agrees to waive its rights and release the other Party from its obligations under paragraph 2 of Article XII of the Treaty.

(3) Notwithstanding any provision of the Treaty, no funds may be drawn from the Treasury of the United States of America for payments under paragraph 4 of Article XIII without statutory authorization.

(4) Any accumulated unpaid balance under paragraph 4(c) of Article XIII of the Treaty at the date of termination of the treaty

shall be payable only to the extent of any operating surplus in the last year of the duration of the Treaty, and nothing in such paragraph may be construed as obligating the United States of America to pay, after the date of the termination of the Treaty, any such unpaid balance which shall have accrued before such date.

(5) Exchange of the instruments of ratification of the Panama Canal Treaty and of the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal shall not be effective earlier than March 31, 1979, and such Treaties shall not enter into force prior to October 1, 1979,

unless legislation necessary to implement the provisions of the Panama Canal Treaty shall have been enacted by the Congress of the United States of America before March 31, 1979.

(6) After the date of entry into force of the Treaty, the Panama Canal Commission shall, unless otherwise provided by legislation enacted by the Congress of the United States of America, be obligated to reimburse the Treasury of the United States of America, as nearly as possible, for the interest cost of the funds or other assets directly invested in the Commission by the Government of the United States of America and for

the interest cost of the funds or other assets directly invested in the predecessor Panama Canal Company by the Government of the United States of America and not reimbursed before the date of entry into force of the Treaty. Such reimbursement for such interest costs shall be made at a rate determined by the Secretary of the Treasury of the United States of America and at annual intervals to the extent earned, and if not earned, shall be made from subsequent earnings. For purposes of this reservation, the phrase "funds or other assets directly invested" shall have the same meaning as the phrase "net direct

investment" has under section 62 of title 2 of the Canal Zone Code.

(b) UNDERSTANDINGS:

(1) Before the first day of the three-year period beginning on the date of entry into force of the Treaty and before each three-year period following thereafter, the two Parties shall agree upon the specific levels and quality of services, as are referred to in paragraph 5 of Article III of the Treaty, to be provided during the following three-year period and, except for the first three-year period, on the reimbursement to be made for the costs of such services, such services to be limited to such as are essential to

the effective functioning of the Canal operating areas and the housing areas referred to in paragraph 5 of Article III. If payments made under paragraph 5 of Article II for the preceding three-year period, including the initial three-year period, exceed or are less than the actual costs to the Republic of Panama for supplying, during such period, the specific levels and quality of services agreed upon, then the Panama Canal Commission shall deduct from or add to the payment required to be made to the Republic of Panama for each of the following three years one-third of such excess or deficit, as the case may be. There shall be an

independent and binding audit, conducted by an auditor mutually selected by both Parties, of any costs of services disputed by the two Parties pursuant to the reexamination of such costs provided for in this understanding.

(2) Nothing in paragraph 3, 4, or 5 of Article IV of the Treaty may be construed to limit either the provisions of the first paragraph of Article IV providing that each Party shall act, in accordance with its constitutional processes, to meet danger threatening the security of the Panama Canal, or the provisions of paragraph 2 of Article IV providing that the United States of America

shall have primary responsibility to protect and defend the Canal for the duration of the Treaty.

(3) Nothing in paragraph 4(c) of Article XIII of the Treaty shall be construed to limit the authority of the United States of America, through the United States Government agency called the Panama Canal Commission, to make such financial decisions and incur such expenses as are reasonable and necessary for the management, operation, and maintenance of the Panama Canal. In addition, toll rates established pursuant to paragraph 2(d) of Article III need not be set at levels designed to produce revenues to cover the

payment to the Republic of Panama described in paragraph 4(c) of Article XIII.

(4) Any agreement concluded pursuant to paragraph 11 of Article IX of the treaty with respect to the transfer of prisoners shall be concluded in accordance with the constitutional processes of both Parties.

(6) The President shall include all reservations and understandings incorporated by the Senate in this resolution of ratification in the instrument of ratification to be exchanged with the Government of the Republic of Panama.

The Treaty was ratified by the

President of the United States of America on June 15, 1978, subject to the said reservations and understandings, in pursuance of the advice and consent of the senate and was ratified on the part of the Republic of Panama on June ____, 1978;

It is provided in Article II of the Treaty that the Treaty shall enter into force simultaneously with the Treaty Concerning Permanent Neutrality and Operation of the Panama Canal, six calendar months from the date of the exchange of the instruments of ratification.

The instruments of ratification of the Treaty were delivered to Panama on June 16, 1978, with the exchange of the instruments of ratification effective on

April 1, 1979, and accordingly the Treaty subject to the said reservations and understandings, enters into force on October 1, 1979;

NOW, THEREFORE, I, Jimmy Carter, President of the United States of America, proclaim and make public the Treaty, subject to the said reservations and understandings, to the end that it shall be observed and fulfilled with good faith on and after October 1, 1979, by the United States of America and by the citizens of the United States of America and all other persons subject to the jurisdiction thereof.

IN TESTIMONY WHEREOF, I have signed this proclamation and caused the Seal of the United States of America to be affixed.

DONE at the city of Washington this twenty-fourth day of September in the year of our Lord one thousand nine hundred seventy-nine and of the Independence of the United States of America the two hundred fourth.

By the President:

Warren Christopher
Acting Secretary of State

Jimmy Carter

PANAMA CANAL TREATY

The United States of America and the Republic of Panama,

Acting in the spirit of the Joint Declaration of April 3, 1964,[1] by the Representatives of the Governments of the United States of America and the Republic of Panama, and of the Joint Statement of Principles of February 7, 1974,[2] initialed by the Secretary of State of the United States of America and the Foreign Minister of the Republic of Panama, and

Acknowledging the Republic of Panama's sovereignty over its territory,

Have decided to terminate the prior

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[1]Department of State Bulletin, Apr.27, 1964, p.656

[2]Department of State Bulletin, Feb. 27, 1974, p.184.

Treaties pertaining to the Panama Canal and to conclude a new Treaty to serve as the basis for a new relationship between them and, accordingly, have agreed upon the following:

ARTICLE I

Abrogation of Prior Treaties and Establishment of a New Relationship

1. Upon its entry into force, this Treaty terminates and supersedes:

(a) The Isthmian Canal Convention between the United States of America and the Republic of Panama, signed at Washington, November 18, 1903;[3]

(b) The Treaty of Friendship and Cooperation signed at Washington,

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[3]TS 431; 33 Stat. 2234; 10 Bevans 663.

March 2, 1936,[1] and the Treaty of Mutual Understanding and Cooperation and the related Memorandum of Understandings Reached, signed at Panama, January 25, 1955,[2] between the United States of America and the Republic of Panama;

(c) All other treaties, conventions, agreements and exchanges of notes between the United States of America and the Republic of Panama, concerning the Panama Canal which were in force prior to the entry into force of this Treaty;[3] and

(d) Provisions concerning the Panama Canal which appear in other

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[1]TS 945; 55 Stat. 1807; 10 Bevans 742.

[2]TIAS 3297; 6 UST 3297.

[3]See agreed minute, para. 1.

treaties, conventions, agreements and exchanges of notes between the United States of America and the Republic of Panama which were in force prior to the entry into force of this Treaty.

2. In accordance with the terms of this Treaty and related agreements, the Republic of Panama, as territorial sovereign, grants to the United States of America, for the duration of this Treaty, the rights necessary to regulate the transit of ships through the Panama Canal, and to manage, operate, maintain, improve, protect and defend the Canal. The Republic of Panama guarantees to the United States of America the peaceful use of the land and water areas which it has been granted the rights to use for such purposes pursuant to this Treaty

and related agreements.

3. The Republic of Panama shall participate increasingly in the management and protection and defense of the Canal, as provided in this Treaty.

4. In view of the special relationship established by this Treaty, the United States of America and the Republic of Panama shall cooperate to assure the uninterrupted and efficient operation of the Panama Canal.

ARTICLE II

Ratification, Entry into Force, and Termination

1. This Treaty shall be subject to ratification in accordance with the constitutional procedures of the two Parties. The instruments of ratification of this Treaty shall be exchanged at Panama at the same time as

the instruments of ratification of the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal,[1] signed this date, are exchanged. This Treaty shall enter into force, simultaneously with the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal, six calendar months from the date of the exchange of the instruments of ratification.[2]

2. This Treaty shall terminate at noon, Panama time, December 31, 1999.

ARTICLE III

Canal Operation and Management

1. The Republic of Panama, as territorial sovereign, grants to the

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[1] omitted

[2] Oct. 1, 1979.

United States of America the rights to manage, operate, and maintain the Panama Canal, its complementary works, installations and equipment and to provide for the orderly transit of vessels through the Panama Canal. The United States of America accepts the grant of such rights and undertakes to exercise them in accordance with this Treaty and related agreements.

2. In carrying out the foregoing responsibilities, the United States of America may:

(a) Use for the aforementioned purposes, without cost except as provided in this Treaty, the various installations and areas (including the Panama Canal) and waters, described in the Agreement in

Implementation of this Article,[1] signed this date, as well as such other areas and installations as are made available to the United States of America under this treaty and related agreements, and take the measures necessary to ensure sanitation of such areas;

(b) Make such improvements and alterations to the aforesaid installations and areas as it deems appropriate, consistent with the terms of this Treaty;

(c) Make and enforce all rules pertaining to the passage of vessels through the Canal and other rules with respect to navigation and maritime matters, in accordance with

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[1]TIAS 10031; post. p.141.

this Treaty and related agreements. The Republic of Panama will lend its cooperation, when necessary, in the enforcement of such rules;

(d) Establish, modify, collect and retain tolls for the use of the Panama Canal, and other charges, and establish and modify methods of their assessment;

(e) Regulate relations with employees of the United States Government;

(f) Provide supporting services to facilitate the performance of its responsibilities under this Article;

(g) Issue and enforce regulations for the effective exercise of the rights and responsibilities of

the United States of America under this Treaty and related agreements. The Republic of Panama will lend its cooperation, when necessary, in the enforcement of such rules; and

(h) Exercise any other right granted under this Treaty, or otherwise agreed upon between the two Parties.

3. Pursuant to the foregoing grant of rights, the United States of America shall, in accordance with the terms of this Treaty and the provisions of United States law, carry out its responsibilities by means of a United States Government agency called the Panama Canal Commission, which shall be constituted by and in conformity with the laws of the United States of America.

(a) The Panama Canal Commission shall be supervised by a Board composed of nine members, five of whom shall be nationals of the United States of America, and four of whom shall be Panamanian nationals proposed by the Republic of Panama for appointment to such positions by the United States of America in a timely manner.

(b) Should the Republic of Panama request the United States of America to remove a Panamanian national from membership on the Board, the United States of America shall agree to such a request. In that event, the Republic of Panama shall propose another Panamanian national for appointment by the United States of America to such position in a

timely manner. In case of removal of a Panamanian member of the board at the initiative of the United States of America, both Parties will consult in advance in order to reach agreement concerning such removal, and the Republic of Panama shall propose another Panamanian national for appointment by the United States of America in his stead.

(c) The United States of America shall employ a national of the United States of America as Administrator of the Panama Canal Commission, and a Panamanian national as Deputy Administrator, through December 31, 1989. Beginning January 1, 1990, a Panamanian national shall be employed as the Administrator and a national of the

United States of America shall occupy the position of Deputy Administrator. Such Panamanian nationals shall be proposed to the United States of America by the Republic of Panama for appointment to such positions by the United States of America.

(d) Should the United States of America remove the Panamanian national from his position as Deputy Administrator, or Administrator, the Republic of Panama shall propose another Panamanian national for appointment to such position by the United States of America.

4. An illustrative description of the activities the Panama Canal Commission will perform in carrying out the responsibilities and rights of the

United States of America under this article is set forth at the Annex. Also set forth in the annex are procedures for the discontinuance or transfer of those activities performed prior to the entry into force of this Treaty by the Panama Canal Company or the Canal Zone Government which are not to be carried out by the Panama Canal Commission.

5. The Panama Canal Commission shall reimburse the Republic of Panama for the costs incurred by the Republic of Panama in providing the following public services in the Canal operating areas and in housing areas set forth in the Agreement in Implementation of the Article III of this Treaty and occupied by both United States and Panamanian citizen employees of the Panama Canal

Commission: police, fire protection, street maintenance, street lighting, street cleaning, traffic management and garbage collection. The Panama Canal Commission shall pay the Republic of Panama the sum of ten million United States dollars ($10,000,000) per annum for the foregoing services. It is agreed that every three years from the date that this Treaty enters into force, the costs involved in furnishing said services shall be reexamined to determine whether adjustment of the annual payment should be made because of inflation and other relevant factors affecting the cost of such services.

6. The Republic of Panama shall be responsible for providing, in all areas comprising the former Canal Zone,

services of a general jurisdictional nature such as customs and immigration, postal services, courts and licensing, in accordance with this Treaty and related agreements.

7. The United States of America and the Republic of Panama shall establish a Panama Canal Consultative Committee, composed of an equal number of high-level representatives of the United States of America and the Republic of Panama and which may appoint such subcommittees as it may deem appropriate. This Committee shall advise the United States of America and the Republic of Panama on matters of policy affecting the Canal's operation. In view of both Parties' special interest in the continuity and

efficiency of the Canal operation in the future, the Committee shall advise on matters such as general tolls policy, employment and training policies to increase the participation of Panamanian nationals in the operation of the Canal, and international policies on matters concerning the Canal. The Committee's recommendations shall be transmitted to the two Governments, which shall give such recommendations full consideration in the formulation of such policy decisions.

8. In addition to the participation of Panamanian nationals at high management levels of the Panama Canal Commission, as provided for in paragraph 3 of this Article, there shall be growing participation of Panamanian

nationals at all other levels and areas of employment in the aforesaid Commission, with the objective of preparing, in an orderly and efficient fashion, for the assumption by the Republic of Panama of full responsibility for the management, operation and maintenance of the Canal upon the termination of this Treaty.

9. The use of the areas, waters and installations with respect to which the United States of America is granted rights pursuant to this Article, and the rights and legal status of United States Government agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in Implementation of this Article, signed

this date.

10. Upon entry into force of this Treaty, the United States Government agencies known as the Panama Canal Company and the Canal Zone Government shall cease to operate within the territory of the Republic of Panama that formerly constituted the Canal Zone.

ARTICLE IV

Protection and Defense

1. The United States of America and the Republic of panama commit themselves to protect and defend the Panama Canal. Each Party shall act, in accordance with its constitutional processes, to meet the danger resulting from an armed attack or other actions which threaten the security of the Panama Canal or of ships transiting it.

2. For the duration of this Treaty, the United States of America shall have primary responsibility to protect and defend the Canal. The rights of the United Sates of America to station, train, and move military forces within the Republic of Panama are described in the Agreement in Implementation of this Article, signed this date.[1] The use of areas and installations and the legal status of the armed forces of the United Sates of America in the Republic of Panama shall be governed by the aforesaid Agreement.

3. In order to facilitate the participation and cooperation of the armed forces of both Parties in the protection and defense of the Canal, the

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[1]TIAS 10032; post, p. 307.

United States of America and the Republic of Panama shall establish a Combined Board comprised of an equal number of senior military representatives of each Party. These representatives shall be charged by their respective governments with consulting and cooperating on all matters pertaining to the protection and defense of the Canal, and with planning for actions to be taken in concert for that purpose. Such combined protection and defense arrangements shall not inhibit the identity or lines of authority of the armed forces of the United States of America or the Republic of Panama. The Combined Board shall provide for coordination and cooperation concerning such matters as:

(a) The preparation of contingency plans for the protection and defense of the Canal based upon the cooperative efforts of the armed forces of both Parties;

(b) The planning and conduct of combined military exercises; and

(c) The conduct of United States and Panamanian miliary operations with respect to the protection and defense of the Canal.

4. The Combined Board shall, at five-year intervals throughout the duration of this Treaty, review the resources being made available by the two Parties for the protection and defense of the Canal. Also, the Combined Board shall make appropriate recommendations to the two Governments

respecting projected requirements, the efficient utilization of available resources of the two Parties, and other matters of mutual interest with respect to the protection and defense of the Canal.

5. To the extent possible consistent with its primary responsibility for the protection and defense of the Panama Canal, the United States of America will endeavor to maintain its armed forces in the Republic of Panama in normal times at a level not in excess of that of the armed forces of the United States of America in the territory of the former Canal Zone immediately prior to the entry into force of this Treaty.

ARTICLE V

Principle of Non-Intervention

Employees of the Panama Canal Commission, their dependents and designated contractors of the Panama Canal Commission, who are nationals of the United States of America, shall respect the laws of the Republic of Panama and shall abstain from any activity incompatible with the spirit of this Treaty. Accordingly, they shall abstain from any political activity in the Republic of Panama as well as from any intervention in the internal affairs of the Republic of Panama. The United States of America shall take all measures within its authority to ensure that the provisions of the Article are fulfilled.

ARTICLE VI

Protection of the Environment

1. The United States of America and the Republic of Panama commit themselves to implement this Treaty in a manner consistent with the protection of the natural environment of the Republic of Panama. To this end, they shall consult and cooperate with each other in all appropriate ways to ensure that they shall give due regard to the protection and conservation of the environment.

2. A Joint Commission on the Environment shall be established with equal representation from the United States of America and the Republic of Panama, which shall periodically review the implementation of this Treaty and shall recommend as appropriate to the two Governments ways to avoid or, should

this not be possible, to mitigate the adverse environmental impacts which might result from their respective actions pursuant to the Treaty.

3. The United States of America and the Republic of Panama shall furnish the Joint Commission on the environment complete information on any action taken in accordance with this Treaty which, in the judgment of both, might have a significant effect on the environment. Such information shall be made available to the Commission as far in advance of the contemplated action as possible to facilitate the study by the commission of any potential environmental problems and to allow for consideration of the recommendation of the commission before the contemplated action is carried out.

ARTICLE VII

Flags

1. The entire territory of the Republic of Panama, including the areas the use of which the Republic of Panama makes available to the United States of America pursuant to this Treaty and related agreements, shall be under the flag of the Republic of Panama, and consequently such flag always shall occupy the position of honor.

2. The flag of the United States of America may be displayed, together with the flag of the Republic of Panama, at the headquarters of the Panama Canal Commission, at the site of the combined Board, and as provided in the Agreement in Implementation of Article IV of this Treaty.

3. The flag of the United States of America also may be displayed at other places and on some occasions, as agreed by both Parties.

ARTICLE VIII

Privileges and Immunities

1. The installations owned or used by the agencies or instrumentalities of the United States of America operating in the Republic of Panama pursuant to this Treaty and related agreements, and their official archives and documents, shall be inviolable. The two Parties shall agree on procedures to be followed in the conduct of any criminal investigation at such locations by the Republic of Panama.

2. Agencies and instrumentalities

of the Government of the United States of America operating in the Republic of Panama pursuant to this Treaty and related agreements shall be immune from the jurisdiction of the Republic of Panama.

3. In addition to such other privileges and immunities as are afforded to employees of the United States Government and their dependents pursuant to this Treaty, the United States of America may designate up to twenty officials of the Panama Canal Commission who, along with their dependents, shall enjoy the privileges and immunities accorded to diplomatic agents and their dependents under international law and practice. The United States of America shall furnish

to the Republic of Panama a list of the names of said officials and their dependents, identifying the positions they occupy in the Government of the United States of America, and shall keep such list current at all times.

ARTICLE IX

Applicable Laws and Law Enforcement

1. In accordance with the provisions of this Treaty and related agreements, the law of the Republic of Panama shall apply in the areas made available for the use of the United States of America pursuant to this Treaty. The law of the Republic of Panama shall be applied to matters or events which occurred in the former Canal Zone prior to the entry into force of this Treaty only to the extent

specifically provided in prior treaties and agreements.

2. Natural or juridical persons who, on the date of entry into force of this Treaty, are engaged in business or non-profit activities at locations in the former Canal Zone may continue such business or activities at those locations under the same terms and conditions prevailing prior to the entry into force of this Treaty for a thirty-month transition period from its entry into force. The Republic of Panama shall maintain the same operating conditions as those applicable to the aforementioned enterprises prior to the entry into force of this Treaty in order that they may receive licenses to do business in the Republic of Panama

subject to their compliance with the requirements of its law. Thereafter, such persons shall receive the same treatment under the law of the Republic of Panama as similar enterprises already established in the rest of the territory of the Republic of Panama without discrimination.

3. The rights of ownership, as recognized by the United States of America, enjoyed by natural or juridical private persons in buildings and other improvements to real property located in the former Canal Zone shall be recognized by the Republic of Panama in conformity with its laws.

4. With respect to buildings and other improvements to real property located in the Canal operating areas,

housing areas or other areas subject to the licensing procedure established in Article IV of the Agreement in Implementation of Article III of this Treaty, the owners shall be authorized to continue using the land upon which their property is located in accordance with the procedures established in that Article.

5. With respect to buildings and other improvements to real property located in areas of the former Canal Zone to which the aforesaid licensing procedure is not applicable, or may cease to be applicable during the lifetime or upon termination of this Treaty, the owners may continue to use the land upon which their property is located, subject to the payment of a

reasonable charge to the Republic of Panama. Should the Republic of Panama decide to sell such land, the owners of the buildings or other improvements located there shall be offered a first option to purchase such land at a reasonable cost. In the case of non-profit enterprises, such as churches and fraternal organizations the cost of purchase will be nominal in accordance with the prevailing practice in the rest of the territory of the Republic of Panama.

6. If any of the aforementioned persons are required by the Republic of Panama to discontinue their activities or vacate their property for public purposes, they shall be compensated at fair market value by the Republic of

Panama.

7. The provisions of paragraphs 2-6 above shall apply to natural or juridical persons who have been engaged in business or non-profit activities at locations in the former Canal Zone for at least six months prior to the date of signature of this Treaty.

8. The Republic of Panama shall not issue, act or enforce any law, decree, regulation, or internal agreement or take any other action which purports to regulate or would otherwise interfere with the exercise on the part of the united States of America of any right granted under this Treaty or related agreements.

9. Vessels transiting the Canal, and cargo, passengers and crews carried

on such vessels shall be exempt from any taxes, fees, or other charges by the Republic of Panama. However, in the event such vessels call at a Panamanian port, they may be assessed charges incident thereto, such as charges for services provided to the vessel. The Republic of panama may also require the passengers and crew disembarking from such vessels to pay such taxes, fees and charges shall be assessed on a nondiscriminatory basis.

10. The United States of America and the Republic of Panama will cooperate in taking such steps as may from time to time be necessary to guarantee the security of the Panama Canal Commission, its property, its employees and their dependents, and

their property, the Forces of the United States of America and the members thereof, the civilian component of the United States Forces, the dependents of members of the Forces and the civilian component, and their property, and the contractors of the Panama Canal Commission and of the United States Forces, their dependents, and their property. The Republic of Panama will seek from its Legislative Branch such legislation as may be needed to carry out the foregoing purposes and to punish any offenders.

11. The Parties shall conclude an agreement whereby nationals of either State, who are sentenced by the course of the other State, and who are not domiciled therein, may elect to serve

their sentences in their State of nationality.[1]

ARTICLE X

Employment with the Panama Canal Commission

1. In exercising its rights and fulfilling its responsibilities as the employer, the United States of America shall establish employment and labor regulations which shall contain the terms, conditions and prerequisites for all categories of employees of the Panama Canal Commission. These regulations shall be provided to the Republic of Panama prior to their entry into force.

2. (a) The regulations shall establish a system of preference when

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[1]TIAS 9787; UST p.1565.

hiring employees, for Panamanian applicants possessing the skills and qualifications required for employment by the Panama Canal Commission. The United States of America shall endeavor to ensure that the number of Panamanian nationals employed by the Panama Canal Commission in relation to the total number of its employees will conform to the proportion established for foreign enterprises under the law of the Republic of Panama.

(b) The terms and conditions of employment to be established will in general be no less favorable to persons already employed by the Panama Canal Company or Canal Zone Government prior to the entry into force of this Treaty, than those in effect immediately prior

to that date.

3. (a) The United States of America shall establish an employment policy for the Panama Canal Commission that shall generally limit the recruitment of personnel outside the Republic of Panama to persons possessing requisite skills and qualifications which are not available in the Republic of Panama.

(b) The United States of America will establish training programs for Panamanian employees and apprentices in order to increase the number of Panamanian nationals qualified to assume positions with the Panama Canal Commission, as positions become available.

(c) Within five years from

the entry into force of this Treaty, the number of United States nationals employed by the Panama Canal Commission who were previously employed by the Panama Canal Commission who were previously employed by the Panama Canal Company shall be at least twenty percent less than the total number of United States nationals working for the Panama Canal Company immediately prior to the entry into force of this Treaty.

(d) The United States of America shall periodically inform the Republic of Panama, through the Coordinating Committee, established pursuant to the Agreement in Implementation of Article III of this Treaty, of available positions within the Panama Canal Commission. The

Republic of Panama shall similarly provide the United States of America any information it may have as to the availability of Panamanian nationals claiming to have skills and qualifications that might be required by the Panama Canal Commission, in order that the United States of America may take this information into account.

4. The United States of America will establish qualification standards for skills, training and experience required by the Panama Canal Commission. In establishing such standards, to the extent they include a requirement for a professional license, the United States of America, without prejudice to its right to require additional professional skills and qualifications, shall

recognize the professional licenses issued by the Republic of Panama.

5. The United States of America shall establish a policy for the periodic rotation, at a maximum of every five years, of United States citizen employees and other non-Panamanian employees, hired after the entry into force of this Treaty. It is recognized that certain exceptions to the said policy of rotation may be made for sound administrative reasons, such as in the case of employees holding positions requiring certain non-transferable or non-recruitable skills.

6. With regard to wages and fringe benefits, there shall be no discrimination on the basis on nationality sex, or race. Payments by

the Panama Canal Commission of additional remuneration, or the provision of other benefits, such as home leave benefits, to United States nationals employed prior to entry into force of this Treaty, or to persons of any nationality, including Panamanian nationals who are thereafter recruited outside of the Republic of Panama and who change their place of residence, shall not be considered to be discrimination for the purpose of the paragraph.

7. Persons employed by the Panama Canal Company or Canal Zone Government prior to the entry into force of this Treaty, who are displaced from their employment as a result of the discontinuance by the United States of

America of certain activities pursuant to this Treaty, will be placed by the United States of America, to the maximum extent feasible, in other appropriate jobs with United Sates Civil Service regulations. For such persons who are not United States nationals, placement efforts will be confined to United States Government activities located within the Republic of Panama. Likewise, persons previously employed in activities for which the Republic of Panama assumes responsibility as a result of this Treaty will be continued in their employment to the maximum extent feasible by the Republic of Panama. The Republic of Panama shall, to the maximum extent feasible, ensure that the terms and conditions of

employment applicable to personnel employed in the activities for which it assumes responsibility are no less favorable than those in effect immediately prior to the entry into force of this Treaty. Non-United States nationals employed by the Panama Canal Company or Canal Zone Government prior to the entry into force of this Treaty who are involuntarily separated from their positions because of the discontinuance of an activity by reason of this Treaty, who are not entitled to an immediate annuity under the United States Civil Service Retirement System, and for whom continued employment in the Republic of Panama by the Government of the United States of America is not practicable, will be provided special

job placement assistance by the Republic of Panama for employment in positions for which they may be qualified by experience and training.

8. The Parties agree to establish a system where the Panama Canal Commission may, if deemed mutually convenient or desirable by the two Parties, assign ceratin employees of the Panama Canal Commission, for a limited period of time, to assist in the operation of activities transferred to the responsibility of the Republic of Panama as a result of this Treaty or related agreements. The salaries and other costs of employment of any such persons assigned to provide such assistance shall be reimbursed to the United States of America by the Republic

of Panama.

9. (a) The right of employees to negotiate collective contracts with the Panama Canal Commission is recognized. Labor relations with employees of the Panama Canal Commission shall be conducted in accordance with forms of collective bargaining established by the United States of America after consultation with employee unions.

(b) Employee unions shall have the right to affiliate with international labor organizations.

10. The United States of America will provide an appropriate early optional retirement program for all persons employed by the Panama Canal Company or Canal Zone Government immediately prior to the entry into

force of this Treaty. In this regard, taking into account the unique circumstances created by the provisions of this Treaty, including its duration, and their effect upon such employees, the United States of America shall, with respect to them:

(a) determine that conditions exist which invoke applicable United States law permitting early retirement annuities and apply such law for a substantial period of the duration of the Treaty;

(b) seek special legislation to provide more liberal entitlement to, and calculation of, retirement annuities than is currently provided for by law.

ARTICLE XI

Provisions for the Transition Period

The Republic of Panama shall reassume plenary jurisdiction over the former Canal Zone upon entry into force of this Treaty and in accordance with its terms.

1. In order to provide for an orderly transition to the full application of the jurisdictional arrangements established by this Treaty and related agreements, the provisions of the Article shall become applicable upon the date this Treaty enters into force, and shall remain in effect for thirty calendar months. The authority granted in this Article to the United States of America for this transition period shall supplement, and is not intended to limit, the full application and effect of the rights and authority

granted to the united States of America elsewhere in this Treaty and in related agreements.

2. During this transition period, the criminal and civil laws of the United States of America shall apply concurrently with those of the Republic of Panama in certain of the areas and installations made available for the use of the United States of America pursuant to this Treaty, in accordance with the following provisions:

(a) The Republic of Panama permits the authorities of the United States of America to have the primary right to exercise criminal jurisdiction over United States citizen employees of the Panama Canal Commission and their dependents, and members of the United

Sates Forces and civilian components and their dependents, in the following cases:

(i) for any offense committed during the transition period within such areas and installations, and

(ii) for any offense committed prior to that period in the former Canal Zone.

The Republic of Panama shall have the primary right to exercise jurisdiction over all other offenses committed by such person, except as otherwise provided in this Treaty and related agreements or as may be otherwise agreed.

(b) Either Party may waive its primary right to exercise jurisdiction in a specific case or

category of cases.

3. The United States of America shall retain the right to exercise jurisdiction in criminal cases relating to offenses committed prior to the entry into force of this Treaty in violation of the laws applicable in the former Canal Zone.

4. For the transition period, the United States of America shall retain police authority and maintain a police force in the aforementioned areas and installations. In such areas, the police authorities of the United States of America may take into custody any person not subject to their primary jurisdiction if such person is believed to have committed or to be committing an offense against applicable laws or

regulations, and shall promptly transfer custody to the police authorities of the Republic of Panama. The United States of America and the Republic of Panama shall establish joint police patrols in agreed areas. Any arrests conducted by a joint patrol shall be the responsibility of the patrol member or members representing the Party having primary jurisdiction over the person or persons arrested.

5. The courts of the United States of America and related personnel, functioning in the former Canal Zone immediately prior to the entry into force of this Treaty, may continue to function during the transition period for the judicial enforcement of the jurisdiction to be exercised by the

United States of America in accordance with this Article.

6. In civil cases, the civilian courts of the United States of America in the Republic of Panama shall have no jurisdiction over new cases of a private civil nature, but shall retain full jurisdiction during the transition period to dispose of any civil cases, including admiralty cases, already instituted and pending before the courts prior to the entry into force of this Treaty.

7. The laws, regulations, and administrative authority of the United States of America applicable in the former Canal Zone immediately prior to the entry into force for the purpose of the exercise by the United States of

U.S.C. 3612(a)). The organizational structure of the PCC evidences that the United States government controls its operations.

The PCC was established to effectuate governmental purposes. It was created to carry out the responsibilities of the United States under the Panama Canal Treaty for operation of the canal (Pet. App. 24c; Treaty Art. III, ¶ 3). As this Court stated in *Rogers* v. *Graves*, 299 U.S. 401, 406 (1937): "That * * * the creation, management and operation of the [Panama] canal are all governmental functions * * * does not admit of doubt."

There is no private profit associated with the PCC's operation of the Panama Canal. Contrary to petitioner's argument (Pet. 20-21), payments made under the Treaty to the Republic of Panama do not qualify as private profit. The PCC collects tolls for the use of the canal (Pet. App. 23c; Treaty Art. III, ¶ 2(d)), the revenues are paid into a United States Treasury fund (22 U.S.C. 3712(c)), and the Republic of Panama is compensated for the Panamanian resources used in the operation of the canal (Pet. App. 77c-80c; Treaty Art. XIII, ¶ 4). The Treaty and federal legislation establishing the PCC provide for no payment of profit to any private entity or individual.

Persons employed by the PCC are not required to be United States government employees in order to be considered "government-connected persons" under *Morse* v. *United States*, 443 F.2d at 1186, and *Kalinski* v. *Commissioner*, 528 F.2d at 973-974. It is sufficient that the employees are subject to federal standards of conduct and discipline and that they are treated similarly to federal employees. *Ibid.* Under this standard, PCC employees are clearly government-connected persons. All PCC Board members, officers, and employees are required to "take an oath to discharge faithfully the duties of his office or employment" (22 U.S.C. 3622(a)).

Every employee is "subject to the laws of the United States regarding duties and responsibilities of Federal employees" (*ibid.*). PCC employees are required to adhere to a code of conduct "substantially equivalent" to that applicable to federal employees. 22 U.S.C. 3622(b). Individual employee grievances concerning job classification and pay rates are reviewed by the Panama Canal Board of Appeals (established pursuant to 22 U.S.C. 3661), and disputes arising between the PCC and its employee unions are handled by the Federal Labor Relations Authority (established pursuant to 5 U.S.C. 7701(b) to regulate rights and obligations of federal government employees).

Because the PCC is a United States agency for purposes of Section 911 of the Internal Revenue Code, the wages received by petitioner's husband from the PCC are subject to federal tax. There is no conflict of decisions or other reason warranting further review.[4]

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[4] Petitioner seeks to raise two additional issues (Pet. i-ii, 26-51): (i) whether the determination that the Panama Canal Commission is a United States agency violates Articles II and IV of the United States Constitution, and (ii) whether the Panama Canal Treaty violates Article II of the United States Constitution. Petitioner did not raise those issues below and the lower courts did not pass on them. Those issues are therefore not properly before the Court. See *Adickes* v. *Kress & Co.*, 398 U.S. 144, 147 n.2 (1970) ("Where issues are neither raised before nor considered by the Court of Appeals, this Court will not ordinarily consider them."). Accord, *United States* v. *Williams*, 112 S. Ct. 1735, 1738 (1992); *Taylor* v. *Freeland & Kronz*, 112 S. Ct. 1644, 1649 (1992); *City of Springfield* v. *Kibbe*, 480 U.S. 257, 266 (1987).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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